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July 2, 2007

Mr. Howard G. Borgstrom
Director, Business Operations Center
Office of the Chief Financial Officer
U.S. Department of Energy
Mailstop CF-60, Room 4A-221
1000 Independence Avenue, S.W.
Washington, DC 20585

Re: Written Comments in Response to RIN 1901-AB21, Loan Guarantees for Projects that Employ Innovative Technologies, 72 *Federal Register* 27471 (May 16, 2007)

Dear Mr. Borgstrom,

In addition to joining in the Joint Comments of Constellation Energy Group, Inc., Entergy Corporation, Exelon Corporation, and NRG Energy, Inc. (NRG) submitted separately today, NRG has prepared the attached mark-up of selected language in the Proposed Rule. NRG hereby submits this mark-up as additional written comments.

Sincerely,

Steve Winn
Executive Vice President
NRG Energy, Inc.

Mark-up of Proposed Rule (Suggested Technical Changes)

The following provides a mark-up of some provisions of the Proposed Rule reflecting strikeouts and inserts to show suggested changes. Following each suggested revision or group of revisions is a brief explanation of the purpose of the suggested change(s).

§ 609.2 Definitions.

Commercial Technology means a technology in general use in the commercial marketplace in the United States, but does not include a technology solely by use of such technology in a demonstration project funded by DOE. A technology is in general use if it: [Alternative 1: has been ordered for, installed in, ~~or~~ and used in five or more projects in the United States] [Alternative 2: has been in operation in ~~a~~three or more commercial projects in the United States for a period of five years, as measured beginning on the date the technology was commissioned on a project.]

If Alternative 1 is selected, then the definition should be linked mostly to the actual "use" of the technology, because ordering or installation is not a valid indicator for proving a new technology that takes many years to build. It is possible that "order" might be said to occur, at least tentatively, before any financing is placed, and partial or even full installation of a technology (over three to five years) will not have proven out the technology until the plant is actually in commercial use. In addition, the limitation in Alternative 2 to one project is inconsistent with the concept of "general" use.

Conditional Commitment means a Term Sheet offered by DOE and accepted by the Applicant, with the understanding of the parties that the Applicant thereafter satisfies all specified and precedent funding obligations, and all other contractual, statutory, regulatory or other requirements. A Conditional Commitment imposes no obligation on the Secretary to execute the Loan Guarantee Agreement, unless the Applicant agrees, at its option, to pay the Credit Subsidy Cost upon issuance.

Once issued, a Conditional Commitment should be a document upon which the various interested parties can rely, similar to a loan commitment, if the Applicant is willing to pay the Credit Subsidy Cost upon issuance

> ***Eligible Lender means:*** ~~*(1) Any*~~ ***any person or legal entity formed for the purpose of, or engaged in the business of, lending money, including, but not limited to, commercial banks, savings and loan institutions, insurance companies, factoring companies, investment banks, institutional investors, venture capital investment companies, trusts, or other entities designated as trustees or agents acting on behalf of bondholders or other lenders;*** ~~*and*~~ ***provided such person or entity meets the requirements of § 609.11 of this part, as determined by DOE.***
>
> ~~*(2) Any person or legal entity that meets the requirements of § 609.11 of this part, as determined by DOE.*~~

This revision eliminates a circularity between the definition and § 609.11.

> ***Eligible Lender Agent or Trustee means the Eligible Lender that is acting as agent bank, placement agent, collateral trustee or indenture trustee on behalf of the Holders.***

The proposed rule should distinguish between any lender and the roles of a Lender Agent, *i.e.*, agent bank, underwriter, collateral trustee or indenture trustee on behalf of the participating lenders or noteholders. This new definition attempts to correct address this.

> ***Eligible Project means a project located in the United States that employs a New or Significantly Improved Technology that is not a*** ~~*commercial technology*~~ ***Commercial Technology, and that meets all applicable requirements of section 1703 of the Act (42 U.S.C. 16513), the applicable solicitation and this part.***

This conforms the language to indicate that this is a defined term.

> ***Guaranteed Obligation means the portion of any loan or other debt obligation of the Borrower for an Eligible Project for which DOE guarantees*** ~~*any part of*~~ ***the payment of principal and interest under a Loan Guarantee Agreement entered into pursuant to the Act.***

At various places in the Rule, "Guaranteed Obligation" is used to mean the entire loan when only the guaranteed portion is intended.

> ***Loan Agreement means a written agreement between a Borrower and one or more Eligible Lenders or other Holders (or an Eligible Lender ~~or other Holder~~ Agent or Trustee on their behalf) containing the terms and conditions under which the Eligible ~~Lender~~ Lenders or other ~~Holder~~ Holders will make loans to the Borrower ~~to start and complete~~ or purchase notes or bonds to finance the construction and ownership of an Eligible Project.***

These changes address the likelihood that a Lender Agent would arrange for the placement of the debt with multiple lenders.

> ***Loan Guarantee Agreement means a written agreement that, when entered into by DOE and a Borrower, and an Eligible Lender Agent or ~~other Holder~~ Trustee, pursuant to the Act, ~~establishes the obligation of DOE to~~ evidences the guarantee by DOE of the payment of principal and interest on specified Guaranteed Obligations of a Borrower to Eligible Lenders or other Holders subject to the terms and conditions specified in the Loan Guarantee Agreement.***

These changes are intended to clarify that there is no further step required after the issuance of the Loan Guarantee Agreement.

> ***New or Significantly Improved Technology means a technology concerned with the production, consumption or transportation of energy, and that has either only recently been discovered or learned, or that involves or constitutes one or more meaningful and important improvements in the productivity or value of ~~the technology~~ a Commercial Technology at the time the guarantee is issued.***

The statutory language provides that the test for new or significantly improved is "as compared to" commercial technologies in service in the U.S. at the time the guarantee is issued.

***Project Costs** means those costs, including escalation and contingencies, that are to be expended or accrued by Borrower and are necessary, reasonable, customary and directly related to the design, engineering, financing, construction, startup, commissioning and shakedown of an Eligible Project, as specified in § 609.12 of this part. ~~Project costs do not include costs for the items set forth in § 609.12(c) of this part.~~*

Costs of credit enhancement are customarily viewed by sponsors and lenders as project costs. Moreover, the exclusion of guarantee costs from Project Costs has the effect of further reducing the 80% guarantee maximum.

§ 609.3 Solicitations.

(c) For projects involving total project costs of $2 billion or more, applications may submitted without solicitation providing the same information as a Pre-Application or Application.

For large projects, the Title XVII program should allow for an open application process.

§ 609.4 Submission of Pre-Applications.

(f) A copy of a ~~commitment~~ letter from an Eligible Lender ~~or other Holder expressing its commitment to provide~~ Agent or Trustee or an investment banking firm of national standing expressing its view that, if a Loan Guarantee Agreement for the Guaranteed Obligations is issued, the required debt financing necessary to construct and fully commission the project can be obtained under current market conditions;

It may not be feasible to have an open-ended loan commitment at this stage of the process, or this commitment will be highly conditional. This change is intended to provide assurance of financeability without requiring a formal loan commitment. In addition, if the financing is done in the bond market, there would be no loan commitment.

§ 609.6 Submission of Applications.

(b)(14) A copy of all material agreements, ~~whether entered into or proposed,~~ to the extent in existence, relevant to the

investment, design, engineering, financing, construction, startup commissioning, shakedown, operations and maintenance of the project;

~~*(15) A copy of the financial closing checklist for the equity and debt;*~~

. . . .

(18) A copy of all ~~*legal opinions, and other*~~ ***material reports, analyses, and reviews related to the project;***

. . . .

(21) A credit assessment, for the project without a ~~*loan guarantee*~~ ***Loan Guarantee Agreement from a nationally recognized rating agency, where the size and estimated cost of the project justify such an assessment, provided, however, that such rating analysis shall be performed without regard for the risks inherent in new technology and, in the case of nuclear generation stations, without regard to potential licensing risk;***

The various agreements referred to, financial closing checklist, and legal opinions may not be available at this early stage of the process. The rating agency review needs to reflect only traditional project risks such as construction, certainty of sales and revenue, and appropriate leverage. The purpose of the Loan Guarantee Agreement is to assist projects that would be difficult to finance due to their utilization of new technology or exposure to uncertain regulatory outcomes. If these conditions are included in the rating agency analysis, the results will be, by definition, unsatisfactory.

§ 609.7 Programmatic, Technical and Financial Evaluation of Applications.

(a)(6) The applicant will not provide a significant equity contribution; provided, however, that for Borrowers that are public power entities DOE may consider and evaluate the merits of project financing structures that do not involve an equity contribution.

. . . .

(b)(7) The amount of equity commitment to the project by the Applicant and other principals involved in the project; provided, however, that for Borrowers that are public power entities DOE may consider and evaluate the merits of project financing structures that do not involve an equity contribution;

Public power entities do not have investors that provide equity, but rather they fund projects based upon the ability to collect funds from ratepayers, which enables such entities to make principal and interest payments for project debt that covers 100% of a project's cost. The rule should provide flexibility to evaluate alternative arrangements proposed by public power entities, which themselves have rate-setting authority that provides a unique source of funds.

609.8 Term Sheets and Conditional Commitments.

(c) The Applicant and/or the Eligible Lender or other Holder may respond to the Term Sheet offer in writing or may request discussions or meetings on the terms and conditions contained in the Term Sheet, including requests for clarifications or revisions. When DOE, the Applicant and the Eligible Lender or other Holder agree on all of the final terms and conditions and all parties sign the Term Sheet, the Term Sheet becomes a Conditional Commitment. When and if all of the terms and conditions specified in the Conditional Commitment have been met, DOE and the Applicant may enter into a Loan Guarantee Agreement, but neither party is legally obligated to do so, except that upon Applicant's payment of the Credit Subsidy Cost the Conditional Commitment shall commit DOE to enter into a Loan Guarantee Agreement for the project if the conditions to the Conditional Commitment are fulfilled prior to the expiration date of the Conditional Commitment, which expiration date shall be no less than twelve months following the issuance of the Conditional Commitment. Any such payment of the Credit Subsidy Cost shall be fully refundable upon notice being given that the conditions have not or will not be met and no guarantee will be issued.

(d) The Applicant is required to pay fees to DOE to cover the Administrative Cost of Issuing a Loan Guarantee for the period of the ~~Term Sheet~~ Conditional Commitment through the closing of the Loan Guarantee Agreement (Second Fee).

One general issue with the proposed rule is that it requires the transaction to be completed and poised for financial closing before a Conditional Commitment is issued. The change here is intended to provide the option of a more customary closing process, in which the credit enhancement commitment would remain in effect for a period of time during which the other closing conditions could be met.

§ 609.9 Closing On the Loan Guarantee Agreement.

(a) Subsequent to entering into a Conditional Commitment with an Applicant, DOE will ~~*set a closing date for*~~ ***execute and deliver the Loan Guarantee Agreement at the financial closing of the project.***

(b) By the financial closing date, the Applicant and the Eligible Lender or other Holder must have satisfied all of the detailed terms and conditions contained in the Conditional Commitment and other related documents and any other contractual, statutory, regulatory or other requirements have been met. ~~*If the Applicant and the Eligible Lender or other Holder has not satisfied all such terms and conditions by the closing date, the Secretary may, in his sole discretion, set a new closing date or terminate the Conditional Commitment.*~~

(c) In order to enter into a Loan Guarantee Agreement at closing:

~~*(1) DOE must have received authority in an appropriations act for the loan guarantee; and*~~

~~*2) All other applicable statutory, regulatory, or other requirements.*~~ ***all*** conditions ***in the Conditional Commitment must be fulfilled.***

It is not practical for DOE to control the closing date. The closing will require a syndication of the financing, which is subject to market condition and industry practice. Variations from standard practice could result in less efficient pricing or terms for the financing. As suggested in comments to Section 609.6(b) above, the Conditional Commitment should provide for a period of time, *e.g.*, six months, for the Lender Agent to make arrangements for

borrowers to participate and then set a financial closing at an appropriate time, taking into consideration of market conditions and other factors. All appropriate conditions to the financial closing, including statutory and regulatory requirements, should be identified in advance and spelled out in the Conditional Commitment so that they are transparent to the lenders in advance.

§ 609.9 Closing On the Loan Guarantee Agreement.

(d)(1) Pursuant to section 1702(b) of the Act, DOE has received payment of the Credit Subsidy Cost of the loan guarantee, as defined in § 609.2 of this part from either ~~*(but not from a combination)*~~ *or both of the following:*

(i) A Congressional appropriation of funds; ~~*or*~~

(ii) A payment from the Borrower;

DOE's prohibition on payment of subsidy cost through combination of borrower payment and appropriations is inconsistent with the Federal Credit Reform Act (FCRA). There is no indication that Congress by providing for self-pay authority intended to eliminate the FCRA provision that incorporates the borrower payment in the calculation of the subsidy cost.

§ 609.9 Closing On the Loan Guarantee Agreement.

(d)(3) OMB has reviewed and approved DOE's calculation of the Credit Subsidy Cost of the loan guarantee. When determining the Credit Subsidy Cost, DOE will evaluate the entire risk profile of project including, but not limited to:

(i) The creditworthiness of the project and project sponsor based on, among other things, the credit rating, if any, of the project sponsor, and other quantitative and qualitative factors such as profitability, liquidity, capital structure, cash flow, default recovery analysis and management and operator experience;

(ii) The Borrower's exposure to market and commodity risks;

(iii) the Borrower's exposure to vendor cost increases or construction delays;

The calculation of the credit subsidy cost needs to be transparent and needs to address the specific risk profile of the project being assessed.

§ 609.9 Closing On the Loan Guarantee Agreement.

(f) Not later than 30 days prior to closing, the applicant must provide a credit rating from a nationally recognized rating agency reflecting the Final Term Sheet for the project without a ~~Federal guarantee~~ Loan Guarantee Agreement provided, however, that such rating analysis shall be performed without regard for the risks inherent in new technology and, in the case of nuclear generation stations, without regard to potential licensing risk.

The rating agency review needs to reflect only traditional project risks such as construction, certainty of sales and revenue, and appropriate leverage. The purpose of the Loan Guarantee Agreement is to assist projects that would be difficult to finance due to their utilization of new technology or exposure to uncertain regulatory outcomes. If these conditions are included in the rating agency analysis, the results will be, by definition, unsatisfactory.

§ 609.10 Loan Guarantee Agreement.

~~(c) Except if explicitly authorized by an Act of Congress, no funds obtained from the Federal Government, or from a loan or other instrument guaranteed by the Federal Government, may be used to pay for Credit Subsidy Costs, administrative fees, or other fees charged by or paid to DOE relating to the Title XVII program or any loan guarantee thereunder.~~

The prohibition on using Federal support to pay subsidy costs or administrative fees is inconsistent with commercial practice and other Federal programs where such fees are routinely financed.

§ 609.10 Loan Guarantee Agreement.

(d)(3) The face value of the debt guaranteed by DOE is limited to no more than 80 percent of total Project Costs ~~and the~~

~~*loan guarantee is limited to no more than 90 percent of the total face value of the loans(s) or other debt obligation(s);*~~

~~*(4) The guaranteed portion of a loan, or any portion of the guaranteed portion of a loan, will not be separated from or "stripped" from the non-guaranteed portion of the loan, if the loan is participated, syndicated or otherwise resold in the secondary debt market;*~~

. . . .

(10) The Borrower has pledged project assets ~~*and other collateral or surety, including non project related assets,*~~ ***determined by DOE to be necessary to secure the repayment of the Guaranteed Obligations, and the Borrower has pledged such other collateral, security and non-project related assets that Borrower at its discretion proposed to reduce the Credit Subsidy Cost for the loan guarantee;***

Title XVII provides for guarantees of loans up to 80% of project cost, and it does not require any additional non-guaranteed debt for the reasons previously discussed. The most common justification for a guarantee of less than 100% of the debt is to encourage lenders to exercise more care in analyzing the credit quality of individual projects. We believe that qualifying lenders have demonstrated a history of exercising care in the evaluation of loans. They will exercise the same level of care under all circumstances as their future fortunes rely on maintaining reputations for integrity and fair dealing. In addition, if the lenders intend to request recovery from the Department of Energy for a failed project, their recovery will depend on their having shown they have exercised their responsibilities with appropriate diligence.

If there is to be non-guaranteed debt, the limitation on stripping substantially decreases the likelihood of successful financing for larger projects. Many investors are prohibited from holding securities with any risk component. If the guaranteed debt is tied to the non-guaranteed debt, a substantial number of investors will be prohibited from investing in the project. This will result in more expensive financings, and increase the potential that projects will not be financed

or completed. In addition, the purchaser of the non-guaranteed, if different from the lender for the guaranteed portion, will provide a second credit analysis. In this respect, stripping provides an additional level of scrutiny for the loan. The guarantee program should recognize the efficiency of the capital markets by allowing the non-guaranteed debt to be priced and sold separately. In addition, there should not be any expectation of collateral beyond the project itself.

609.10 Loan Guarantee Agreement

(d)(5) The Borrower and other principals involved in the project have made or will make a significant equity investment in the project; provided, however, that for Borrowers that are public power entities DOE may consider and evaluate the merits of project financing structures that do not involve an equity contribution;

As noted above, public power entities do not have investors that provide equity, but rather they fund projects based upon the ability to collect funds from ratepayers, which enables such entities to make principal and interest payments for project debt that covers 100% of a project's cost. The rule should provide flexibility to evaluate alternative arrangements proposed by public power entities, which themselves have rate-setting authority that provides a unique source of funds.

609.10 Loan Guarantee Agreement

(d)(7) The loan guarantee does not finance, either directly or indirectly, tax-exempt debt obligations, unless such debt obligations fall within one of the exceptions enumerated in 26 U.S.C. § 149(b)(3)(A), or other similar law.;

Title XVII does not prohibit issuance of loan guarantees for tax-exempt debt obligations, and DOE should not exercise discretion to prohibit such guarantees, if permitted by applicable law.

609.10 Loan Guarantee Agreement

(d)(11) If any of the assets offered by the Borrower as collateral security for the guarantee are subject to prior financing liens by other creditors, DOE will require that such prior lien creditors be removed or an acceptable legal arrangement be made with such prior lien creditors, where DOE will be protected in the event of default. An arrangement of this nature must be in the form of written agreement between DOE and the prior lien creditors, and provide the following conditions:

(i) Ample notice of default and collateral security sale;

(ii) A plan of liquidation offering mutual protection to DOE and other creditors; and

(iii) An option on the part of DOE, which would be assignable to a third party, to have the first lien debt payable according to the original installment terms (even after default) if the project operation is undertaken by DOE or an acceptable third party, or on behalf of or through DOE.

Consistent with DOE's 1980 rulemaking regarding loan guarantees for alternative fuel demonstration facilities, this provision would allow pari passu lien treatment for creditor liens on collateral acquired prior to issuance of the guarantee.

609.10 Loan Guarantee Agreement

(d)(13) The Guaranteed Obligation is not subordinate to any loan or other debt obligation and is in a first lien position on all assets of the project and all additional collateral pledged as security for the Guaranteed Obligations ~~***and other project debt;***~~ ***provided that the Guaranteed Obligations may be pari passu and equal in lien priority with other secured debt on the project and such other collateral to the extent the Guaranteed Obligation and such other secured debt does not exceed, in the aggregate, the maximum amount of Guaranteed Obligations that would be permitted under paragraph(d)(3) of this section.***

This provision would allow DOE to reduce its risk and exposure to the project, guaranteeing an amount less than the maximum amount allowable, by permitting other secured debt that is not guaranteed. Such a structure would allow the government to have the same

security in the assets that it would have if it guaranteed all of the debt but with less risk, because a portion of the risk of default is born by other lenders that do not have any guarantee under this program.

> ***609.10 Loan Guarantee Agreement***
>
> ***(e) The Loan ~~Guarantee~~ Agreement must provide that, in the event of a default by the Borrower:***
>
> ***(1) Interest accrues on the Guaranteed Obligations at the pre-default rate stated in the Loan ~~Guarantee Agreement or Loan~~ Agreement until DOE makes full payment of the defaulted Guaranteed Obligations and DOE is not required to pay any premium, default penalties, or prepayment penalties;***
>
> ***(2) Holders of the Guaranteed Obligations are in first lien position prior to payment of the Guaranteed Obligations by DOE. Upon payment of the Guaranteed Obligations by DOE, DOE is subrogated to the rights of the Holders of the ~~debt~~ Guaranteed Obligations, including all ~~related~~ liens, security, and collateral rights securing the Guaranteed Obligations and has superior rights in and to the property acquired from the recipient of the payment as provided in § 609.15 of this part.***
>
> ....
>
> ***(g) The Loan Guarantee Agreement must contain provisions related to the assignment or transfer of Guaranteed Obligations which provide that:***
>
> ***(1) The Eligible Lender must provide written notification to DOE prior to any assignment or transfer of any portion of a Guaranteed Obligation to a person or entity that is not an eligible assignee, as provided in the Loan Agreement, or any pledge or other use of a Guaranteed Obligation as security, including but not limited to any derivatives transaction.***

The above change regarding the Loan Agreement conform the rule to the apparent intent of the proposed rule. In addition, language regarding DOE's subrogation rights should be revised to allow for security to be taken by the non-guaranteed portion of the debt. Moreover,

restrictions regarding an eligible assignment of the debt should be included in the Loan Agreement, because most investors will require free transferability of the debt. In particular, if a bond structure is used, prior notice of transfer is not feasible. Also, language should be added to clarify that the holders of the guaranteed obligations are secured by the first priority liens until payment on the guarantee, at which point DOE would be subrogated to those rights.

> ***609.11 Lender Eligibility, Monitoring and Performance Requirements.***
>
> ***(a)(4) Be legally authorized to enter into loan guarantee transactions authorized by the Act and these regulations and is in good standing with DOE and other Federal agency loan guarantee programs;***
>
> ***(b) An Eligible Lender Agent or Trustee shall be an Eligible Lender that meets the following requirements:***
>
> ***(1) ~~(5)~~ Be able to demonstrate, or has access to, experience in originating and servicing loans for commercial projects similar in size and scope to the project under consideration; and***
>
> ***(2) ~~(6)~~ Be able to demonstrate experience or capability as the lead lender or underwriter by presenting evidence of its participation in other energy-related projects.***
>
> ***(c) ~~(b)~~ When performing its duties to review and evaluate a proposed Eligible Project prior to the submission of a Pre-Application or Application, as appropriate, by the Project Sponsor through the execution of a Loan Guarantee Agreement, and subsequently when performing the loan servicing duties during the term of the Loan Guarantee Agreement, the Eligible Lender Agent or Trustee ~~other servicer~~ shall exercise the level of care and diligence that a similarly situated agent or trustee reasonable and prudent lender would exercise when reviewing, evaluating, disbursing and servicing a loan made by it without a Federal guarantee, including:***
>
> ***(1) During the construction period, enforcing all of the conditions precedent to all loan disbursements, as provided in the Loan Guarantee Agreement, Loan Agreement and related documents;***

(2) During the operational phase, monitoring and servicing the Debt Obligations and collection of the outstanding principal and accrued interest ~~as well as ensuring that the collateral package securing the Guaranteed Obligations remains uncompromised~~; and

(3) ~~As specified by DOE, providing annual or more frequent financial aid and other reports on the status and condition of the Guaranteed Obligations and the Eligible Project, and~~ pPromptly notifying DOE if it becomes aware of any problems or irregularities concerning the Eligible Project or the ability of the Borrower to make payment on the Guaranteed Obligations or other debt obligations.

(d) ~~(c)~~ Even though DOE may rely on the Eligible Lender Agent or Trustee ~~other servicer~~ to service and monitor the Guaranteed Obligation, DOE will also conduct its own monitoring and review of the Eligible Project.

Several of these changes are intended to set forth obligations and qualification of a lead lender, the Lender Agent or Trustee, as compared to other participating lenders. Also, it is standard in loan documentation for the agent and other lenders to limit their liability except in the case of gross negligence and willful misconduct (and often only as finally determine by a court). The standard in the NOPR is not conventional and will likely limit the numbers of lenders interested in participating in the program. It is not realistic to expect lenders to assume greater liability, especially in the case of a federal loan guarantee program where profit margins are expected to be very limited. In addition, the monitoring and reporting obligations are not consistent with standard practice in capital markets transactions.

§ 609.12 Project Costs

(c) Project Costs do not include:

~~(1) Fees and commissions charged to Borrower, including finder's fees, for obtaining Federal or other funds;~~

. . . .

~~*(7) Borrower-paid Credit Subsidy Costs and the Administrative Cost of Issuing a Loan Guarantee; and*~~

~~*(8) Expenses incurred after startup, commissioning, and shakedown before the facility has been placed in service*~~

(8) Expenses incurred after commercial operation of the facility, except to the extent used to fund reserves to cover interest and amortization during schedule or unscheduled operating outages.

As noted above, costs of credit enhancement are customarily viewed by sponsors and lenders as project costs. Moreover, the exclusion of guarantee costs from Project Costs has the effect of further reducing the 80% guarantee maximum. Finally, the rule should contemplate common features of project finance structures for large industrial projects, where there will likely be requirements for reserves to mitigate against risks of outages.

§ 609.15 Default, Demand, Payment, and Collateral Liquidation.

(a) In the event that the Borrower has defaulted in the making of required payments of principal or interest on any portion of a Guaranteed Obligation, and such default has not been cured within the period of grace provided in the Loan Guarantee Agreement and/or the Loan Agreement, the Eligible Lender or other Holder, or nominee or trustee empowered to act for the Eligible ~~Lender~~ Lenders or other ~~Holder~~ Holders (referred to in this section collectively as "Holder"), may make written demand upon the Secretary for payment pursuant to the provisions of the Loan Guarantee Agreement.

(b) In the event that the Borrower is in default as a result of a breach of one or more of the terms and conditions of the Loan Guarantee Agreement, note, mortgage, Loan Agreement, or other contractual obligations related to the transaction, other than the Borrower's obligation to pay principal or interest on the Guaranteed Obligation, as provided in paragraph (a) of this section, the Holder will not be entitled to make demand for payment pursuant to the Loan Guarantee Agreement, unless the Secretary agrees in writing that such default has materially affected the rights of the parties, and finds that the Holder should be entitled to receive payment pursuant to the Loan Guarantee Agreement. This provision shall not limit

the Holder's right to declare the principal amount of the debt due and payable in advance of its scheduled maturity by reason of such non-monetary default to the extent permitted under the Loan Agreement.

(g) The Loan Guarantee Agreement shall provide that, upon payment of the Guaranteed Obligations, the Secretary shall be subrogated to the rights of the Holders and shall have superior rights in and to the property acquired from the Holders. The Holder shall transfer and assign to the Secretary all rights held by the Holder of the Guaranteed Obligation. Such assignment shall include ~~all~~ any related liens, security, and collateral rights securing the Guaranteed Obligations.

If a non-monetary default reaches the point that the lenders accelerate the debt, the guarantee should be available. This is particularly true because the lenders are in a "first loss" position regarding the non-guaranteed portion of the debt, so any defaults on maintenance, *etc.*, would redound to their detriment.

§ 609.15 Default, Demand, Payment, and Collateral Liquidation.

(k) In addition to foreclosure and sale of collateral pursuant thereto, the U.S. Attorney General shall take appropriate action in accordance with rights contained in the Loan Guarantee Agreement to recover costs incurred by the Government as a result of the defaulted loan or any other defaulted obligation. Any recovery so received by the U.S. Attorney General on behalf of the Government shall be applied in the following manner: First to the expenses incurred by the U.S. Attorney General and DOE in effecting such recovery; second, to reimbursement of any amounts paid by DOE as a result of the defaulted obligation; third, to any amounts owed to DOE under related principal and interest assistance contracts; and fourth, to any other lawful claims held by the Government on such process. Any sums remaining after ~~full~~ pari passu payment of the foregoing shall be available for the benefit of other parties lawfully entitled to claim them.

DOE has misinterpreted the "superior rights" provision [Sec. 1702(g)(2)(B)] as prohibiting *pari passu* financing structures and prohibiting any holders of non-guaranteed debt from recovering on their debt until DOE's claim is paid in full.

§ 609.16 Perfection of Liens and Preservation of Collateral

(a) The Loan Guarantee Agreement and other documents related thereto shall provide that: (1) the Eligible Lender Agent or ~~other Holder~~ Trustee or other servicer will take those actions necessary to perfect and maintain liens, as applicable, on assets which are pledged as collateral for the guaranteed portion of the loan; and (2) upon default by the Borrower, the holder of pledged collateral shall take such actions as the Secretary may reasonably require (provided funds are made available for such actions) to provide for the care, preservation, protection, and maintenance of such collateral so as to enable the United States to achieve maximum recovery from the pledged assets. The Secretary shall reimburse the holder of collateral for reasonable and appropriate expenses incurred in taking actions required by the Secretary. Except as provided in § 609.15, no party may waive or relinquish, without the consent of the Secretary, any collateral securing the Guaranteed Obligation to which the United States would be subrogated upon payment under the Loan Guarantee Agreement.

These minor changes are suggested to clarify the role of the Lender Agent or Trustee, and to provide assurance that it will be compensated for action taken on behalf of the government.

§ 609.17 Audit and Access to Records

(a)(3) Prior to any disbursement of funds during construction from a loan subject to a Loan Guarantee Agreement, an independent engineer shall have reviewed and provided a certification of the costs. In the absence of fraud, once disbursed pursuant to such procedures, such disbursed loan amounts shall be subject to the guarantee.

(b) The Secretary may from time to time audit any or all items of costs included as Project Costs in statements or certificates submitted to the Secretary or the servicer or otherwise, ~~and may exclude or reduce the amount of any item which the Secretary determines to be unnecessary or excessive, or otherwise not to be an item of Project Costs.~~ The Borrower

will make available to the Secretary all books and records and other data available to the Borrower in order to permit the Secretary to carry out such audits. The Borrower should represent that it has within its rights access to all financial and operational records and data relating to Project Costs, and agrees that it will, upon request by the Secretary, exercise such rights in order to make such financial and operational records and data available to the Secretary. In exercising its rights hereunder, the Secretary may utilize employees of other Federal agencies, independent accountants, or other persons.

The prospects of after-the-fact auditing and disallowance of specific disbursements by DOE are not practical for implementing the loan guarantee program. Rather, Lenders require assurance that when their funds are disbursed they will be done so appropriately and subject to the both the financing arrangements and the Loan Guarantee Agreement. The only practical way for this to occur is to follow accepted industry practice, which would provide for an independent engineer that reviews and certifies the costs.